BRIEF IN SUPPORT OF PETITION.

Opinions Below.

The opinion of the Circuit Court of Appeals was handed down on February 4, 1942, and has not yet been officially reported. It appears on pages 51 to 61 of the Record. The opinion of the District Court is reported in 37 Fed. Supp. 822, and appears at pages 34 to 37 of the Record.

Jurisdiction.

This Court has jurisdiction under section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

Statement of the Case.

Massachusetts is one of a number of states whose legislatures have authorized the formation of non-profit hospital service corporations to be operated on a charitable basis. The plaintiff is so incorporated (R. 35).

It appears from its by-laws (R. Exhs. B and C) and from the findings (R. 37) that the plaintiff has no shareholders, stockholders or other forms of beneficial interest in any individual or corporation. Its voting members are representatives of hospitals, the medical profession and the general public (R. 52). Its officers and directors have served without compensation (R. 53).

The plaintiff makes contracts with and receives money from members of the public who are subscribers. It makes contracts with and pays money to hospitals for care of its subscribers. The administration of these activities is the whole of plaintiff's business.

The subscriber's contracts (R. Exhs. F and G) are for a one-year period with privilege of termination by either

party and have no provisions for assessment from or refund to subscribers. If the funds of the plaintiff are not sufficient to pay hospital bills, the hospital contracts (R. Exhs. D and E) require acceptance by the hospitals of a proportion. Full responsibility by hospitals for the fulfillment of subscriber contracts is therefore required (R. 40).

There cannot be profits in the usual sense of the term. Any excess of receipts over disbursements for a given period may be used to make up an excess of hospitalization over receipts in another period. There is and can be no refund of subscribers' contributions.

These facts are stated in the District Court opinion (R. 34-36) and in the Circuit Court opinion (R. 52-54). The only misstatement in the latter is (R. 54) that "membership . . . is composed largely of the middle class and well-to-do." The evidence does not support this statement. It appears in the subscriber's contract (R. Exh. G) that the plaintiff has a ward plan to appeal to the income bracket of $1000 to $2000 a year on a low rate basis. The testimony (R. 42), which the trial judge accepted (R. 34), was: "We were and now are primarily interested in that great middle class of people who find it most difficult to meet the cost of hospitalization. The indigent are adequately provided for; the well-to-do can afford hospitalization." Obviously the appeal of these plans is to the middle class worker who has $100 or $200 to pay bills but the payment of which upsets his budget. By these plans people of small or moderate means are able in large measure to pay their bills and keep the self-respect which is an attribute of a good citizen. And obviously the interest of the state is to encourage a plan which will lead its people away from the temptation to avoid hospitals and hospital bills until it is too late.

We submit that this kind of organization may fairly be called a charity in the sense in which Congress uses that term.

Specification of Errors.

The Circuit Court of Appeals erred—

1. In holding that the plaintiff is not a corporation organized and operated for charitable purposes.

2. In disregarding the command of the Massachusetts legislature that for the plaintiff to exist it must qualify as a charity.

3. In refusing to Massachusetts the right to fix the character of its corporations.

4. In holding the plaintiff is a business corporation.

5. In ignoring the declaration of Congress that a similar corporation operating in the District of Columbia is a charitable corporation.

6. In failing to follow the law of Massachusetts in determining the attributes of the plaintiff.

7. In reversing the decision of the District Court.

Summary of Argument.

The characteristics of the plaintiff are fixed by state law. The Massachusetts legislature has required that an organization incorporated under its chapter 176A have the characteristics of a charity. The law of the United States and the law of Massachusetts as to what constitutes a charity are in harmony. Therefore the legislative condition that the plaintiff incorporate and operate like a charity requires it to incorporate and act like a charity in conformity with a law which is like the law of the United States.

The characteristics of the plaintiff being fixed by state law, the Federal tax result depends on these characteristics. Congress intended to exempt from tax organizations having the characteristics of a charity in accordance with Federal law. The plaintiff has these characteristics.

Tax laws are to be uniformly interpreted throughout the country. The decision of the Circuit Court here creates lack of uniformity in the light of both the special Act of Congress and decisions in other circuits.

This is a matter of public importance to a kind of community organization which has greatly expanded in recent years.

Argument.

1. It is familiar law in our Federal system that state law creates the rights, privileges and characteristics of persons within the jurisdiction of the state. This has been emphasized of late by the change of interpretation of section 34 of the Federal Judiciary Act of September 24, 1789 (U.S. Code, Title 28, sec. 725). When, therefore, the Massachusetts legislature requires, as it does in section 10 of chapter 176A of the General Laws, that every hospital service plan be a charity, it requires such a plan to assume the attributes and characteristics of a charity. As was said in *Harrison* v. *Barker Annuity Fund*, 90 Fed. (2d) 286 (C.C.A. 7): "The corporation was organized for one purpose and one only and that special grant of authority from the state conclusively estops it from exercising any other powers."

There can be no question that the plaintiff operates within the terms of its charter. The trial judge so found (R. 35) and the entering into subscriber and hospital contracts is required in terms by General Laws, chapter 176A, section 1.

The remaining question is whether the characteristics of a charity under Federal law are similar to those under Massachusetts law. This Court and the Supreme Judicial Court of Massachusetts have a common background of long-decided cases as to what constitutes a charity and the re-

lationship of the sovereign and the chancery court to a charity. Some of these cases, citing as authority and being cited with approval by the other court of last resort, are:

Russell v. *Allen*, 107 U.S. 163.
Jones v. *Habersham*, 107 U.S. 174.
The Late Corporation of Latter Day Saints v. *United States*, 136 U.S. 1.
Hopkins v. *Grimshaw*, 165 U.S. 342.
Sohier v. *Wardens of St. Paul Church*, 12 Met. 250.
Saltonstall v. *Sanders*, 11 Allen, 446.
Jackson v. *Phillips*, 14 Allen, 539.
Old South Society v. *Crocker*, 119 Mass. 1.

These cases are all landmarks in the law of charities and enunciate like principles. When an organization qualifies as a charity under Massachusetts law it qualifies also under Federal law, for these laws are the same. And when the plaintiff is required by Massachusetts law to act as a charity and acts in that way, it is a charity under Federal law.

This is not like the cases where state law applies different nomenclature from that of Congress to similar things, as for example in—

Burk-Waggoner Oil Association v. *Hopkins*, 269 U.S. 110.
Palmer v. *Bender*, 287 U.S. 551.
Morgan v. *Commissioner*, 309 U.S. 78.

This is a case where the substantial rights and duties created by the state law must be recognized in the administration of Federal tax laws.

Poe v. *Seaborn*, 282 U.S. 101.
Blair v. *Commissioner*, 300 U.S. 5.
Helvering v. *Fuller*, 310 U.S. 69.

2. The ultimate test of a charity under the Social Security law was intended to be the use to which its income is applied.

H. Rep. No. 615, 74th Congress, 1st Session, pp. 21-22 and 32-33.

This may be income from commercial operations.

Trinidad v. *Sagrada Orden de Predicadores,* 263 U.S. 578.

It is common knowledge that the large charitable organizations in this country conduct business and manage real estate to produce money to further their charitable ends. This plaintiff does nothing more than conduct a hospital insurance business, with its surplus, if any, to be used for members in a future period or applied *cy près.* The present surplus is obviously accumulated to pay hospital bills in time of epidemic or other calamity. That period, sure to come if history is believed, will be the testing hour of the plaintiff and Congress intended that its potentiality should not be reduced by the payment of Federal taxes.

The statement of the majority in the opinion of the Circuit Court that subscribers do not join the plaintiff with any donative intent (R. 56) is irrelevant.

Union Pacific Railway Co. v. *Artist,* 60 Fed. 365 (C.C.A. 8).

Charities conduct many business relationships with persons who have no donative intent. The application of the surplus of the charity is the only thing that counts. The plaintiff has no profits in the ordinary sense of surplus disposable at will. Its surplus belongs to the sovereign that created it.

The argument that surplus on liquidation will be applied *cy près* is dismissed by the majority of the Circuit Court on the ground that liquidation while solvent is extremely unlikely (R. 56). The proposal of the President of the United States in his 1942 budget message to include hospitalization insurance as a part of an enlarged Social Security program suggests a likely reason for liquidation if such proposal becomes law. In the meantime, it is submitted, the effort of the states to work out a plan of hospitalization insurance on a voluntary basis through the means of a private charity under the supervision of state officials is deserving of the encouragement afforded to charities in the tax acts.

3. Taxing acts are to be construed so as to be uniformly applied throughout the country.

Heiner v. *Mellon,* 304 U.S. 271.

There is no such uniformity as a result of the decision here and the decision referred to in the petition holding mutual benefit associations to be charitable.

Gimbel v. *Commissioner,* 54 Fed. (2d) 780.
Mutual Aid & Benefit Association v. *Commissioner,* 42 Fed. (2d) 619.
Harrison v. *Barker Annuity Fund,* 90 Fed. (2d) 286.

Under the Circuit Court decision here a gift to the plaintiff would not be a proper deduction in computing income tax (R. 59). Yet the plaintiff, open to enough people in the community and looking to their better health, is certainly a charity in the broad sense as used in the Gimbel case. A gift to the plaintiff would be exactly like a gift to a hospital —it would help take care of that indefinite class who may be sick tomorrow.

There is no uniformity when the Eighth Circuit Court in *Union Pacific Railway Co.* v. *Artist,* 60 Fed. 365, at page 369, relying on *Jackson* v. *Phillips,* 14 Allen, 539, holds a company plan for hospitalization to be charitable while the Circuit Court of Appeals here holds a state-wide plan not to be charitable.

There can be no such uniformity when the Congress has specifically defined an organization similar in all respects to the plaintiff as a charity and exempted it from the taxes which the Circuit Court says were properly collected from the plaintiff. Section 8 of the Act creating "Group Hospitalization, Inc.," (quoted in full *supra,* p. 5), certainly shows Congressional appreciation of the motives actuating the Massachusetts legislature in enacting section 10 of chapter 176A of the General Laws (quoted *supra,* p. 2) and of the 18 other state legislatures declaring such corporations charitable (Appendix B, p. 16).

There can be no Congressional reason for attempting to differentiate between hospital service plans in the states and in the District of Columbia.

Respectfully submitted,

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